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REPORT
No. 98-234

UNIFORM SINGLE AUDIT ACT OF 1983

SEPTEMBER 22 (legislative day, SEPTEMBER 19), 1983.—Ordered to be printed

Mr. DURENBERGER, from the Committee on Governmental Affairs, submitted the following

REPORT

[To accompany S. 1510]

The Committee on Governmental Affairs, to which was referred the bill (S. 1510) to establish uniform single financial audit requirements for State and local governments and nonprofit organizations and other recipients of Federal assistance, and for other purposes, having considered the same, reports favorably thereon with an amendment in the nature of a substitute and recommends that the bill as amended do pass.

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I. Introduction and Background

Our system of Government today rests on an elaborate structure of interlocking relationships among all levels of government for managing Federal assistance programs. A number of ways exist to help assure that those entrusted with the responsibility for administering Federal assistance are fully accountable. This includes program monitoring by Federal program officers; Quality Assurance and Control Programs exercised by the Federal assistance recipients; and audits conducted of the Federal assistance recipients. Auditing plays an important part in the accountability process, and covers a wide range of audit activities. This includes financial audits, audits of specific compliance with terms and requirements of specific programs, or audits to determine whether specific programs are being operated economically, efficiently, and effectively. These audits are defined and discussed in the "Standards for Audit of Governmental Organizations, Programs, Activities, and Functions," issued by the Comptroller General of the United States. This wide range of audit activities highlights the importance for a clear understanding of the scope of audit required and what the audit will and will not provide the users of the audit results.

One of the major problems concerning the current audit of Federal assistance is the lack of a clear definition or understanding of what is to be achieved from the audit. This legislation is intended to provide for a uniform single audit of the recipient of Federal assistance.

In an attempt to present a clear understanding of the Single Audit concept, the following sections have been prepared to provide the readers basic understanding and history of this concept.

THE ORIGINAL AUDIT PROBLEM

Beginning in the early 1970's, the General Accounting Office (GAO) and the Office of Management and Budget (OMB) became concerned about the Federal Government's control over grant programs and audits in particular. In 1979, GAO completed a study that produced some significant findings. The study found that a very large number of the State and local governments handling Federal funds never had their grant transactions audited. Some 80 to 90 percent of the $70 billion dispersed to State and local governments each year were not audited sufficiently. A few governments, however, always seemed to be under audit. GAO argued that the principal cause of this situation was the manner in which the audit work was organized. Rather than look at organizations as a whole, auditors audited on a grant-by-grant basis. This grant-by-grant auditing often exposed the entity to multiple audits continually disrupting the entity and hampering program efforts.

In February of 1979, the Joint Financial Management Improvement Project (JFMIP) in its report, "Audit of Federally Assisted Programs: A New Emphasis," stated that:

> Duplication and overlap of audit effort are most prevalent at the local government level. Duplication and overlap occur when different audit organizations audit an entity within the same period and review the same accounting records, internal controls,

and policies; contact the same personnel; and audit the same organizational segments of an entity. They also occur when an audit of a grant is made and the audit is subsequently determined as inadequate, causing the auditors to reaudit the same grant covering essentially the same areas.

Gaps in audit coverage exist at all levels. Gaps occur primarily from the failure of auditors to assess compliance with grant requirements, but also from infrequent audits of certain Federal programs. Finally, the report concluded by stating that:

> We believe the answer lies in Federal agencies adopting the single audit approach to auditing federally assisted programs. This would provide for a single financial and compliance audit of a recipient covering all the recipient's funds. The audit would be regularly conducted on an organization-wide basis to assess the fiscal integrity of financial transactions and to assess compliance with grant requirements. The latter would involve, for example, checking whether eligibility requirements had been met, grant funds had been spent for the intended service of product, cost allocations had been proper, direct charges had been reasonable, and any matching requirements had been met.
>
> The single audit approach would not substitute for other reviews, such as economy and efficiency audits, program results reviews, investigative audits, program monitoring, and other special audits directed toward a specific overall Federal program rather than toward individual grants and individual recipients. A substantial portion of Federal audit effort is directed toward individual grant audits. With the adoption of the single audit approach, more emphasis could be placed on performing these above audits.

The report went on to say it is intended that one audit will be performed to satisfy all the interests of the Federal Government, and that since many agencies may be involved in financing a State, or local governmental entity one agency should be assigned to supervise the single audit of the entity on behalf of all other Federal agencies and departments.

II. Legislative History

IMPLEMENTING THE SINGLE AUDIT

On October 22, 1979, the Office of Management and Budget (OMB) responded to reports of uncoordinated and ineffective audit and reporting techniques employed by the Federal Government with attachment P to Circular A–102.

Attachment P to Circular A–102, "Uniform Requirements for Grants to State and Local Governments," established a new approach to auditing of Federal aid programs. In the past, audits were made on a grant-by-grant basis resulting in overlap and duplication. Under the new "single audit" approach, State and local governments were to obtain a single organization-wide audit encompassing all Federal grants. Circular A–110, attachment F, applies principles similar to those contained in attachment D but applies to nonprofit organizations and universities.

The Circular contains general policy guidance with regard to how single audits should be made. To further aid with the implementation of the Circular, OMB provided the audit community the "Compliance Supplement for Single Audits of State and Local Governments." The supplement presents information on the major compliance features of 60 programs that make up over 90 percent of Federal aid to State and local governments. In the foreword to the compliance supplement, OMB Director, David Stockman stated:

> The use of this document in conjunction with the standard audit guide will facilitate a "single audit" that will encompass the needs of all users and will enable State and local governments to meet the Federal Governments' need for assurance of compliance with applicable laws and regulations. It is expected that this will result in a more appropriate sharing of audit responsibilities among the levels of government, and further streamline the intergovernmental grants system.

He went on to say:

> The implementation of the single audit is consistent with the Administration's Federalism program in that it permits State and local governments to use their own procedures to demonstrate accountability for Federal funds while reducing Federal intrusion.

The Committee on Governmental Affairs has found, however, that implementation of attachment P has been less than satisfactory. The Committee understands that this is a complex and very difficult process to implement nationwide. However, the problem of uncoordinated, overlapping and duplicating auditing of Federal grants remains. The Committee has concluded that enactment of the "Uniform Single Audit Act of 1983" (Senate bill 1510), will provide the necessary statutory base for the Single Audit concept, and achieve the uniformity nationwide this concept needs to be successful.

III. Section-by-Section Analysis

A. SECTION 7501. PURPOSES

The purposes of this chapter are to—

(1) improve the financial management of Federal assistance programs;

(2) promote the efficient use of audit resources;

(3) help relieve State and local governments and nonprofit organizations of the costs and paperwork burdens due to conflicting, redundant, and unreasonable audit requirements of Federal assistance programs;

(4) provide for the establishment of consistent and uniform requirements for financial audits of State and local governments and nonprofit organizations and other recipients of Federal assistance;

(5) specify standard financial audit requirements for Federal assistance programs established after the date of enactment of this chapter;

(6) to have the audit requirements of this chapter phased in and met by each entity that receives Federal assistance within three years from the enactment of this legislation; and

(7) to have Federal agencies and departments, in planning and performing any additional work, to the maximum extent feasible, rely upon and not duplicate work done pursuant to this chapter.

B. SECTION 7502. DEFINITIONS

This section defines the following terms: (1) "Federal agency and department;" (2) "entity;" (3) "Federal assistance;" (4) "generally accepted government auditing standards;" (5) "independent auditors;" (6) "public accountants;" (7) "State;" (8) "Indian tribe;" (9) "local government;" (10) "nonprofit organization;" (11) "recipient;" (12) "single audit;" and (13) "cognizant agency." These terms are self-explanatory, except for the following:

Paragraph (2) defines the term "entity" to mean a State government, a local government, or a nonprofit organization, or a recipient of Federal assistance. The Committee recognizes that in some cases, State and local governments may find it difficult in the beginning to perform an organization-wide audit, encompassing all of their departments and agencies and may prefer to conduct audits on a departmental or agency-wide basis. However, the Committee expressly intends that such entities adopt an organization-wide audit procedure as a more efficient and effective method of implementing the requirements of this act, and that the identification of the entity for audit be consistent with generally accepted accounting principles and standards.

Paragraph (3), "Federal assistance" means any assistance provided by a Federal agency or department to an entity in the form of grants, loans, loan guarantees, and cooperative agreements. Types of Federal assistance that would be affected includes, but is not limited to, project grants, formulas grants, categorical grants, block grants, and General Revenue Sharing. An example of a loan would be an Unemployment Compensation loan to a State. A cooperative agreement could be a joint research effort between the Federal Government and a university.

Paragraph (4), "Generally Accepted Government Auditing Standards" contains the definition of a financial and compliance audit of an entity receiving Federal assistance. These standards are issued by the Comptroller General and incorporate the generally accepted auditing standards issued by the AICPA. These standards are subject to change and all such changes, affecting the financial and compliance element shall be followed by independent auditors during the performance of audits.

Paragraph (6) "Public accountant," defines who is eligible to perform audits involving Federal assistance. It is the express intent of the Congress to be consistent with the recommendations made by the Comptroller General of the United States. The recommendation defines those public accountants qualified to perform an audit of Federal assistance. The recommendation is set forth by the Comptroller General in the "Standards for Audit of Governmental Organizations, Programs, Activities and Functions."

Paragraph (10) defines a "nonprofit organization" as those organizations described in section 501(c) of the internal revenue code and

those organizations described in State statutes covering nonprofit organizations. The Committee recognizes that the definition of a nonprofit organization is not always clearly definable, thus it is the Committee's intent that the term means an organization which is primarily operated for scientific, educational, charitable, or some similar purpose in the interest of the public; is not established with making a profit as the primary goal and objective; and uses its proceeds to maintain, improve or expand its activities. Some nonprofit organizations because of the nature of their operations, might be considered similar to a commercial concern for purposes of accounting and in the application of cost principles. The independent auditor should take this into consideration during the audit.

Paragraph (12) defines a single audit. A single financial audit means an audit conducted by an independent auditor in accordance with the auditing standards for the financial and compliance element of the generally accepted government auditing standards issued by the Comptroller General of the United States. The audit is to determine and report on whether an entity's financial statements present fairly the financial position and the results of financial operations of the entity in accordance with generally accepted accounting principles; whether the entity has complied with laws and regulations that may have a material effect upon the financial statements; and whether the entity has in place internal controls that can provide reasonable assurance that it is managing its programs in compliance with all applicable laws and regulations. This audit should provide Federal agencies and departments with reasonable assurance that a recipient of Federal assistance has provided financial data that can be relied upon, has internal controls in place and functioning for controlling the receipt and expenditure of Federal assistance funds, has complied with the significant terms and conditions of major Federal assistance programs, and that the recipient's claims for assistance were proper and supportable.

It is important in understanding the single audit report to be aware of what such an audit will and will not provide the user.

The single audit will:

1. Include an examination of an entity's financial statements;
2. Be made on an entity-wide basis covering all funds;
3. Determine if statements present fairly the financial position and the results of financial operations in accordance with generally accepted accounting principles. This will include a determination as to whether
   (a) the accounting principles selected and applied are generally accepted, and are otherwise appropriate for use under the circumstances;
   (b) the financial statements are informative on matters that may affect their use, understanding, and interpretation and the information presented in such statements is classified and summarized in a reasonable manner; and
   (c) the financial statements reflect the underlying events and transactions.
4. Help satisfy the general financial audit needs of all users of the entity's financial statements;

5. Result in a written report on whether statements present fairly the financial position and the results of financial operations and whether the statements were presented in accordance with generally accepted accounting principles. If an unqualified (positive) opinion cannot be expressed, the auditor must state the reasons therefore;

6. Study and evaluate the entity's internal controls. Internal controls are the plan of organization and methods and procedures adopted by management to ensure that resource use is consistent with laws, regulations, and policies; that resources are safeguarded against waste, loss, and misuse; and that reliable data are obtained, maintained, and fairly disclosed in reports. The study and evaluation is to:

(a) ascertain the level of reliance that can be placed on the internal controls to establish a basis for determining the extent of audit testing that is necessary as a step in forming an opinion on the financial statements, and

(b) determine whether the internal controls in place provide reasonable assurance that the entity is complying with the laws and regulations.

7. Provide a written report on the study and evaluation of internal controls, identifying as a minimum

(a) the entity's significant controls;

(b) the controls that were studied and evaluated;

(c) the controls that were not studied and evaluated, and the reasons therefore; and

(d) the material weaknesses identified as a result of the study and evaluation.

(8) Determine whether the entity complied with laws and regulations that could materially affect the entity's financial statements. In testing for Federal compliance the auditor must use the total Federal assistance as a basis for determining the necessary materiality level, rather than the total assistance as reported in the financial statements. This will result in some audit coverage of Federal, State, local and other assistance, respectively. It should be noted that this would not include an evaluation of the program's economy, efficiency, and effectiveness nor would it necessarily provide detailed information on compliance with specific program requirements;

9. Result in a written report on the results of compliance testing, including a statement that, of those items tested, the entity was or was not in compliance with applicable laws and regulations. If, during or in connection with the audit, auditors become aware of fraud, abuse or illegal acts, or indications of such acts, they shall report such acts in accordance with generally accepted government auditing standards;

10. Assure more overall audit coverage of Federal funds than was previously attained under the grant-by-grant audit approach; and

11. Serve as a building block or basis for conducting additional work in the area of program compliance, economy, efficiency, program results and program evaluation.

The Single Audit, however, will not:

1. Examine the economy and efficiency of the entity's operations, or ascertain whether the desired program results or benefits are being achieved.

2. Assure that all financial compliance requirements or nonfinancial compliance requirements contained in laws and regulations applicable to each of the audited entity's grants are examined.

3. Assure that each Federal grant is tested during the audit.

4. Guarantee the discovery of all fraud, abuse, or illegal acts that might have been committed.

5. Necessarily cover all the audit requirements contained in special user documents such as Attachment P to A–102, issued by the Office of Management and Budget.

In addition to steps which may be taken to assure the financial integrity of an entity administering Federal assistance, and to provide reasonable assurance that program funds are spent in accordance with applicable law, periodic reviews of the economy and efficiency of specific program management can be made. Such reviews would be performed in accordance with the standards for economy and efficiency audits included in the Standards for Audit of Governmental Organizations, Programs, Activities, and Functions, issued by the Comptroller General.

The scope of such a review would be tailored to the role of the entity and the nature of the program operations it is carrying out. At a minimum, however, it would focus on the extent to which the entity is acquiring resources economically and using those resources efficiently in carrying out program operations. Depending on the agency or department and the program, this may necessitate reviewing personnel practices, procurement practices, organizational structure, and planning and budgeting systems. If the entity operates the program through subrecipients or contractors, the review would include an examination of the entity's system for monitoring the performance of such third parties. In each case, the report of the review would identify opportunities for improvement and make appropriate recommendations to overcome identified weaknesses. It should be left to the discretion of the entity whether the various elements will be covered in a single review or in a series of separate reviews. Upon completion of each review, the resulting report would be made public and a copy forwarded to the appropriate Federal agency or department.

A requirement of this type would give Congress some assurance of continuing attention to matters of managerial efficiency in the implementation of the programs it funds. However, the funding of such audit requirements would have to be addressed by the Congress.

In addition to reviews of management economy and efficiency, assessments can be made of the effectiveness of the program. The objectives could be left to the discretion of the entity, in consultation with the appropriate Federal agency or department.

To satisfy the requirement, an entity would have to develop an evaluation plan which defined the performance measures to be used in the evaluation and an approach to collecting and analyzing data. The plan would be submitted for review and comment by the admin-

istering Federal agency or department prior to implementation. Upon completion of the evaluation, the resulting report would be made public and a copy forwarded to the administering Federal agency or department.

A requirement of this type would give Congress some assurance of continuing attention to the effectiveness of the programs it funds, and would provide a reasonably reliable source of information about whether or not the programs are accomplishing their intended purposes. However, the funding for this requirement would have to be addressed by the Congress. See appendix A for suggested language provided to the Committee by the General Accounting Office.

Paragraph (13) defines the role of the cognizant agency. This chapter requires that in planning and performing any evaluations or audits of recipients of Federal assistance, the Federal agencies and departments, to the extent feasible, shall rely upon and not duplicate the single audit. This chapter also requires that work performed by or for the Federal agencies and departments shall be coordinated in order to coincide, to the extent feasible, with the performance of the single audit.

To help accomplish this coordination and to prevent numerous Federal audit organizations and/or contracted independent auditors from overlapping and duplicating audit efforts of the entities, this chapter requires that the Office of Management and Budget, in consultation with the appropriate government officials, shall designate Federal agencies or departments to be cognizant for the recipients of Federal assistance. The Office of Management and Budget currently has developed a cognizant system as part of the implementation of OMB Circular A–102, attachment P. The system developed by OMB originally assigned different cognizant agencies to individual State departments and larger local governments within a State. Subsequently, OMB assigned, for a limited number of State governments, a single cognizant agency. For the purposes of this chapter, OMB, unless determined not to be feasible after consultation with the appropriate government officials, should assign a single Federal cognizant agency for all recipients of Federal assistance within a State.

C. SECTION 7503. PROMULGATION OF POLICIES, PROCEDURES AND REGULATIONS

This section provides for the implementation of this chapter.

Paragraph (a) and (b) of this section provide the President, or the Director of the Office of Management and Budget, with the responsibility for promulgating policies, procedures and regulations. The President or the Director may delegate the authority to prescribe regulations to appropriate Federal agencies and departments. However, in the preparation of policies, procedures and regulations, the President or Director, and all affected Federal departments and agencies, shall consult with the Comptroller General of the United States.

Paragraph (c) requires the Office of Management and Budget in consultation with the Comptroller General and other State and local government and nonprofit officials to establish a plan of action within 1 year of the date of this legislation to assure that required audits are

completed within 3 years from the date of enactment of this legislation and thereafter. While this provision requires the Office of Management and Budget to establish an implementation plan within 1 year, the Committee believes that this can be done within 6-months or sooner from the date of enactment of the legislation. OMB currently has similar audit requirements and implementing plans in place and should have little difficulty in establishing a plan of action to implement the audit provisions of this chapter. While the committee does not wish to dictate the contents of the plan, we suggest, as a minimum, that the plan include (1) a system for identifying those entities that must follow the provisions of the chapter and (2) a system for obtaining feedback on completed audits.

It is also the intent of the committee that the audits be phased in over the 3-year period rather than waiting until the third year to complete the audits. The committee believes that since most of the State governments and large local governments and nonprofit organization currently have financial audits conducted either annually or at least biennially, these entities will be able to meet the provisions of the chapter with the audit preceding the enactment of this legislation. Those other entities can be phased in prior to the end of the 3-year period.

While it is not a provision of this chapter, the committee believes that OMB should prepare in consultation with the appropriate Federal, State, local, and nonprofit officials, a listing of suggested financial compliance requirements similar to the current OMB compliance supplement, except expanded to cover all domestic Federal assistance programs. While this listing would be for information purposes only, independent auditors in testing for compliance with Federal laws and regulations could use, at their discretion, the listing.

Paragraph (d) requires that OMB in consultation with the Comptroller General and other State and local government and nonprofit officials, establish a plan of action to coordinate any audit and evaluation work contracted for or conducted by the Federal agencies and departments. This work includes, but is not limited to, economy and efficiency audits, program results audits, program evaluations, and in-depth compliance testing. It is the intent of the committee that the single audit serve as a basis, or as a building block, by the Federal agencies and departments for performing further audit work or evaluation work. Also, it is the intent of the committee that work be coordinated by the cognizant agency assigned for such purposes and to the extent feasible coincide with the performance of the single audit.

D. SECTION 7504. AUDIT REQUIREMENTS

Single audit

The single audit provisions of S. 1510 contain a number of important factors. First, the audit must cover all of the funds of the entire entity being audited, not just the Federal assistance funding. This approach permits orderly coverage of all funds in one audit thus avoiding disruption, duplication and overlapping of audit efforts. This chapter defines the entity as a State government, a local government, or a nonprofit organization, or a recipient of Federal assistance from any of the foregoing. While the chapter has a provision that

permits the entity to have an audit by department or agency, rather than of the entire entity, certain conditions must exist for this to be permitted. For example, the department or agency must have its own general purpose financial statements, accounting system, and internal control systems or in other words the entity must meet the definition of an entity set forth in generally accepted accounting standards and principles. However, it is not the intent of this chapter to prevent audits of the individual department and agencies as part of and to be tied into the overall audit of the entity.

Second, the audit must be conducted at least biennially but preferably annually, for each entity that receives Federal assistance for a fiscal year which is equal to or in excess of $25,000, thus providing for audit coverage on a timely basis rather than waiting for extended periods to lapse prior to audits being conducted. Those entities receiving less than $25,000 per year in Federal assistance are not required to have audits made. The intent of this threshold provision is to obtain sufficient audit coverage of those entities receiving the majority of Federal assistance, while exempting those numerous entities receiving small amounts of Federal assistance from the audit provisions of this chapter and other audit requirements currently in existence. While the audit may be conducted biennially covering the entire 2 year period, it is preferred that the audit be conducted annually which is considered to be the most effective way to audit.

During the last several years, both the number and the dollar amounts of government programs and activities have increased substantially at the State and local level. This has brought an increased demand for full accountability by those entrusted with the responsibility for administering the programs and activities. Public officials at these levels of government have recognized that an independent financial audit is an integral element of this accountability and have established their own financial audit requirements. Independent audits of their financial statements and operations are now being conducted on a regular basis by several State and local governments and non-profit organizations, while others have plans to conduct these audits.

Third, the audits must be conducted by independent auditors as defined in generally accepted government auditing standards for qualified external government auditors and public accountants and in accordance with generally accepted government auditing standards. Requiring that the audits be conducted by independent auditors in accordance with generally accepted government auditing standards helps assure that auditors will be objective and nonbiased in their performance of the audits and that the quality of the audit results will be enhanced. It is important that the auditors be free from impairments to their independence, and free to audit and report on the results of the audit without interference.

Fourth, the audit must include a study and evaluation of and report on the extent and condition of internal controls existing within the entity. The audit must describe whether the entity has internal control systems in place to provide reasonable assurance that it is managing Federal programs in compliance with laws and regulations. This study, evaluation, and report should determine whether internal control systems are properly designed and in place to protect the integrity

of all funds received and whether the controls are functioning as management intended.

While it is not the intent of the Committee that the auditor render an opinion on the overall internal control system, the auditors' report should identify as a minimum the entity's significant internal controls in place and the weaknesses in these controls; describe the controls identified that were studied and evaluated, identify the controls that were not studied and evaluated; and report on the material weaknesses identified relative to the controls studied and evaluated. Sufficient information should be included in the report in order to provide Federal agencies, State and local officials and others with a basis to conclude whether the entity had internal control systems in place to provide reasonable assurance that it was managing Federal programs in compliance with laws and regulations. If the audition concludes that internal controls might not provide reasonable assurances that the entity is managing Federal programs in compliance with laws and regulations, or that internal controls are nonexistent, these facts would alert both the entity and the Federal agencies and departments, so that appropriate actions could be taken. This would be one basis for the Federal agencies and departments to conduct or contract for additional audit work on the entity.

Fifth, while the audit must include a determination as to whether the entity has complied with laws and regulations that may have a material effect upon the financial statements, the committee has established fund source universes for testing overall compliance with financial requirements and has in certain instances, established materiality levels for specific testing of Federal expenditures. It is the intent of the committee that in testing compliance with laws and regulations, the individual sources of funding (e.g. total funds received from all Federal sources whether received directly or indirectly) will be the universe for testing for Federal compliance, not the combined total of all sources of funds reflected in the financial statements. The committee believes that this will provide more adequate financial compliance coverage of the respective fund sources, e.g. Federal, State, local, and other. However, the committee wishes to emphasize that the dollar materiality level selected for transaction testing shall be based on the professional judgment of the independent auditor, except in instances where Federal expenditures during a fiscal year are equal to-or exceed $500,000 or 3 percent of the entities' total Federal expenditures, whichever is the greater, or any Federal assistance program for which $30,000,000 or more was expended during the fiscal year.

The Committee intends by setting these materiality levels, that testing Federal compliance will help assure that those entities receiving large amounts of Federal assistance will result in adequate coverage of Federal funds.

The independent auditor in testing compliance with Federal laws and regulations may use the listing of suggested financial compliance requirements prepared by the Office of Management and Budget in consultation with Federal, State, local, and nonprofit officials.

Sixth, the chapter requires that the single financial audit report shall be made available to Federal officials upon request, and unless restricted by law or regulation, copies of reports shall be made available for public inspection. While the provisions of the chapter do not re-

quire the Federal officials to establish a system for submitting each completed report to the appropriate Federal officials, nor does the chapter require the report be reviewed by the appropriate Federal officials, the provisions do not prohibit such a system and review from being established and implemented.

Seventh, the chapter provides that each entity receiving Federal assistance from Federal agencies and departments and subsequently making a portion ($25,000 or more) of the Federal assistance available to another entity, shall have the responsibility for ascertaining whether a single financial audit has been conducted on the recipient. It is not the intent of the committee to hold the entity responsible for assuring that the audit is made of the entity receiving the pass-through funds. However, if an entity receiving pass-through funds has not and/or does not intend to have such an audit conducted, the entity awarding the pass-through funds should notify in writing the Office of Management and Budget. If the entity receiving the pass-through funds is not covered under the provisions of the chapter, the entity awarding the funds should rely upon the professional judgment of the independent auditor as to whether these funds should be tested during the audit of the entity awarding the pass-through funds pursuant to this chapter. Likewise the provisions of this chapter do not limit the recipient from determining through audit or program monitoring that the subrecipient is complying with Federal laws and regulations.

Eight, it is not the intent of this chapter to limit the authority of Federal agencies and departments to conduct or contract for audits and evaluations of Federal assistance programs, but instead to establish uniform audit requirements for recipients of Federal assistance. It is also the intent of the Committee that no additional audit requirements are to be levied by regulation on recipients of Federal assistance.

E. SECTION 7505. PAYMENT FOR PERFORMANCE

When the issue of reimbursement is discussed, two fundamental problems associated with it arise. The first problem that must be addressed is what is the Federal governments "Fair share of the cost of the audit." The second problem is how do independent auditors receive payment for this work.

Studies have shown that many units of government and nonprofit organizations, on a recurring basis (annually, biennially, etc.), have audits conducted of their financial statements. The requirement for this audit is generally provided by a State statute, local law or Federal requirement. The point is that many entities are already required to conduct an audit of their financial statements.

In a 1979 report by the joint financial improvement program entitled "Report on Audit of Federally Assisted Programs: A New Emphasis," the report stated:

We recommend that OMB and the interagency group establish a system for reimbursing the Federal Government's share of single recipient audits.

Discussion

Auditing serves as a management tool for both the grantee and the grantor; therefore, it is the grantor's responsibility to share the audit

costs. Currently, FMC 74–4 permits audit cost as an allowable cost under the grant.

However, under the present approach to auditing federally assisted programs, some problems concerning reimbursement of audit cost have been encountered. Adoption and implementation of the single audit approach would eliminate some of these. However, at least two major problems must still be resolved:

First, a fair and workable mechanism for paying the Federal grantor's fair share of the cost of the single audit must be found.

Second, the obstacles facing some state and local auditors which prevent them from using and accepting reimbursement of costs for audits of federally assisted programs must be removed.

The latter problem is one that must be solved by the individual state and local auditor. Our recommendation addresses the former.

Those commenting on this recommendation agreed almost unanimously that a reimbursement system was a must. There was also a general consensus that the system must be kept as simple as possible for it to be feasible. However, there was no overall agreement of what system was needed or was best.

Approach for implementing recommendation

We recommend that OMB and the interagency group consider the following approach for reimbursing the audit:

The current practice of allowing part of grant funds to be used for audit purposes would be continued. However, the recipient (primary and subgrantee) would be required to certify that funds had been budgeted and would be reserved for financing part of the required single audit.

The cost of the audit would be shared on the basis of funding received; e.g., if the total Federal funds received were 40 percent of the total, 40 percent of the audit cost would be shared by the various Federal grantors. The Federal share would be allocated among the various Federal agencies on the basis of value of grants; e.g., if the Department of Health, Education and Welfare's grant funds were 10 percent of total Federal funds, it would absorb 10 percent of the audit cost.

The cognizant agency during its oversight review would ascertain whether the audit coverage had been proper. The review would assure that the Federal grantors were paying their fair share.

Also in this section, a formula is provided for the purpose of determining that dollar amount which is the maximum amount of resources that can be charged to an individual grant or program for auditing purposes. This amount should be made available to auditors by Federal program managers or recipients of Federal assistance. This amount shall be the maximum amount made available from any Federal grant or program for the audit purposes. In on case shall the amount charged to any Federal grant or program exceed the amount arrived at under this section. This amount is not intended to pay for or defray other audit costs incurred by the entity, such as the audit costs related to state grants or foundation awards or other such assistance.

F. SECTION 7506. SANCTIONS

This section authorizes the Office of Management and Budget to arrange to have conducted any audit work necessary because of an entity's failure to comply with the audit requirements of this chapter. Also, this section provides for the payment of such audit cost out of the allowable administrative cost portion of the Federal assistance received by the entity.

It is not the intent of the committee to use Federal assistance funds to pay for these audits that would normally be used to benefit the individual beneficiaries or to accomplish the purpose of the assistance, but to use that portion of the assistance to pay the audit cost allowed for entity management. The intent is that the sanctions be placed on entity management not the beneficiary.

G. SECTION 7507. SMALL BUSINESS CONCERNS

While this section does not set aside a percentage of the audit work, that might be contracted out to Public Accounting Firms, for the small business concerns and business owned and controlled by socially and economically disadvantaged individuals, it is the intent of the committee to provide the maximum practicable opportunity for these business concerns to participate in the audits pursuant to this chapter.

H. SECTION 7508. RELATIONSHIP TO OTHER LAW

This chapter is not intended to supersede State or local laws, regulations or policies governing the performance of Financial audits. However, this chapter shall be the new standard for all previously enacted financial audit requirements by Congress. This standardization will provide for more efficient and economical financial audit reporting.

LEGISLATION MANDATING AUDIT REQUIREMENTS

This section sets up a new responsibility for the General Accounting Office. The GAO will monitor all bills and resolutions introduced in Congress that contain financial audit requirements. If the financial audit requirements contained in such bills or resolutions are inconsistent with the provisions set forth under this chapter, the Comptroller General shall report by letter at the earliest possible date his finding and alert the Committee on Government Operations of the House of Representatives, or the Governmental Affairs Committee of the Senate. The respective committees will then have to decide what, if any, action they wish to take.

The committee intends to take this oversight role seriously and hopes that all future legislation which contains financial audit requirements will not deviate from the provisions set forth under this chapter.

IV. Evaluation of Regulatory Impact

Paragraph 11(b)(1) of Rule XXVI requires each report accompanying a bill to evaluate "the regulatory impact which would be incurred in carrying out the bill."

S. 1510, as amended, will reduce the total number of Federal regulations and legislative requirements through consolidation and standardization of current legislative and regulatory financial audit requirements and reduce the need for financial audit requirements in future legislation. The Committee notes that some new regulations will be promulgated, but the overall effect will be a reduction in the number of Federal regulations and legislative requirements associated with the financial audit of Federal assistance programs. Promulgation of this legislation and regulations and guidelines pursuant to this legislation will satisfy a far larger number of legislative requirements, regulations, and guidelines currently in existence as well as reduce the need for individual financial audit requirements in future Federal assistance legislation. This chapter also exempts those entities receiving less than $25,000 in Federal assistance from the audit requirements of this chapter. This provision has a regulatory impact in that numerous small recipients of Federal assistance are no longer impacted by current regulations and/or legislation requiring financial audits. The net effect of this chapter will be a reduction in the number of Federal legislative requirements and regulations through issuance of uniform audit requirements that will replace several nonstandard legislative requirements, regulations and guidelines currently in use, and reduce the need for the creation of nonstandard financial audit requirements in future legislation.

V. Estimated Cost of Legislation

U.S. Congress,
Congressional Budget Office,
Washington, D.C., September 7, 1983.

Hon. William V. Roth,
Chairman, Committee on Governmental Affairs, U.S. Senate, Dirksen Senate Office Building, Washington, D.C.

Dear Mr. Chairman: Pursuant to Section 403 of the Congressional Budget Act of 1974, the Congressional Budget Office has reviewed S. 1510, the Uniform Single Financial Audit Act of 1983, as ordered reported by the Senate Committee on Governmental Affairs, August 3, 1983. This bill would require a single, uniform, comprehensive audit, at least biennially, of the funds of state and local governments and nonprofit organizations that receive federal assistance of at least $25,000 annually. This comprehensive audit would replace the various auditing requirements associated with individual grants. Thus, a community receiving a number of federal grants will now be required to conduct one comprehensive financial audit, rather than several financial audits of individual grants.

Currently, most costs for auditing grant programs are included as an administrative expense that can be paid out of grant funds. The bill requires federal departments and agencies that require financial audit work in excess of that included in the independent uniform audit to arrange and pay for such additional effort. If this provision is used extensively, there could be additional costs to the federal government. The potential cost of the provision cannot be estimated, because the extent to which agencies will require additional financial audits cannot be determined. However, agencies are not expected to require a signifi-

cant amount of additional audit work, and the cost of this provision is not expected to be significant.

Under provisions of various state laws, most local governments are currently required to conduct financial audits similar to those required by the bill. To the extent that duplicative activities by state and local governments are reduced, or that additional audit work is paid for by the federal government, there may be some cost savings to state and local governments as a result of this bill. These savings are not expected to be substantial.

Should the committee so desire, we would be pleased to provide further details on this estimate.

Sincerely,

RUDOLPH G. PENNER, *Director.*

VI. ROLLCALL VOTE IN COMMITTEE

In compliance with paragraph 7(c) of rule XXVI of the Standing Rules of the Senate, the rollcall vote taken during Committee consideration of this legislation is as follows:

Final passage. Ordered reported, 13 yeas; 9 nays.

Yeas (13)	Nays (0)
Percy	
Stevens	
Durenberger	
Danforth	
Cochran	
Eagleton	
Chiles	
Nunn	
Glenn	
Sasser	
Levin	
Bingaman	
Roth	

VII. CHANGES IN EXISTING LAW

Rule XXVI of the Standing Rules of the Senate requires that changes in existing law made by the bill, as reported, be detailed in the Committee Report accompanying the bill. No changes in existing law are necessitated by S. 1510, as amended.

APPENDICES

Appendix A

Following is suggested language for the latter two types of reviews.

OPTIONAL LANGUAGE FOR ECONOMY, EFFICIENCY AND COMPLIANCE EVALUATIONS

Each entity receiving funds under this chapter shall evaluate and report upon the efficiency, and economy of its program, and review compliance with program requirements.[1] Such evaluation shall be made public and transmitted to the appropriate Federal agency or Department at least once every 3 years or at such other less frequent intervals as the Federal official on a case-by-case basis may prescribe,[2] provided, however, that evaluations conducted under this subsection shall not be required to be performed as part of a single audit described pursuant to this chapter.[3] Upon request of an entity, the Federal official may waive in whole or in part and for good cause shown requirements for the compliance component of the evaluation described in this paragraph.

Evaluations carried out under this subsection shall be conducted in accordance with the Standards for Audits of Governmental Organizations, Programs, Activities, and Functions issued by the Comptroller General.[4] Plans for conducting the required evaluations shall be submitted to the appropriate Federal official for review and comments.

OPTIONAL REQUIREMENT FOR PROGRAM EFFECTIVENESS EVALUATIONS

Each entity receiving funds under this chapter shall evaluate and report upon the effectiveness and results of its program on some established cycle.[5] [6]

[1] This evaluation would determine (1) whether the recipient managed and utilized its resources (such as personnel, property, space) economically and efficiently, (2) the causes of inefficiences or uneconomical practices, and (3) whether laws and regulations were being complied with. Depending on congressional information needs, the Committee may wish not to include this evaluation requirement or, alternatively, may desire to narrow the scope of the evaluation by striking certain components thereof. For example, there may be a strong congressional information need for information on the program's efficiency and economy, but not for detailed program-specific compliance data. If that is the case, the language calling for a "review of compliance with program requirements" should be deleted.

[2] The frequency of the evaluation would be a matter solely within the discretion of the Congress.

[3] The determination whether to cover these ancillary matters as part of the single audit of the entity or incident to a separate evaluative effort would be left to the discretion of each entity.

[4] This does not require that economy, efficiency, and compliance evaluations be conducted by an entity or persons independent of the recipient, nor does it require that the recipient use its internal auditors to perform such evaluations. These evaluations could be performed by auditors, consultants, analysts, or program evaluators who are external or internal to the entity. However, if the Congress desired evaluations to be conducted by persons or organizations who are independent of the entity, the requirement would be modified accordingly.

[5] This evaluation would determine whether the desired results, objectives, or benefits of the program envisioned by the Congress or the entity are being achieved.

[6] The frequency of the evaluation is a matter solely within the discretion of the Congress.

Such evaluation reports shall be made public and transmitted to the Secretary provided, however, that evaluations conducted under this subsection shall not be required to be performed as part of a audit pursuant to this chapter.[7]

Evaluations carried out under this subsection shall be conducted in accordance with the Standards for Audits of Governmental Organizations, Programs, Activities, and Functions issued by the Comptroller General.[8] State plans for conducting the required evaluations shall be submitted to the Secretary for review and comment."

[7] The determination whether to cover these ancillary matters as part of the single audit of the entity or incident to a separate evaluative effort as part is left to the discretion of each entity.

[8] This does not require that evaluations be conducted by an entity or persons independent of the entity, nor does it require that the entity use its internal auditors to perform such evaluations. These evaluations could be performed by auditors, consultants, analysts, or program evaluators who are external or internal to the recipient. However, if the Congress desired evaluations to be conducted by persons or organizations who are independent of the entity, the requirement would be modified accordingly.

Appendix B

Congressional Research Service,
The Library of Congress,
Washington, D.C., September 7, 1983.

To: Hon. Dave Durenberger.
(Attn: Mike Quaranta)
From: American Law Division.
Subject: Whether Financial Audit Requirements in S. 1510, 98th Congress, the Uniform Single Financial Audit Act of 1983, Conflict with Authority Granted in the Inspector General Act of 1978 (P.L. 95–452).

This memorandum discusses whether the audit requirements imposed by S. 1510 would conflict with authority granted to Inspectors General in Public Law 95–452. The fundamentally different purposes of the bill and act as well as some provisions in S. 1510 suggest that there does not appear to be a conflict. The purposes of S. 1510, among other things, are to establish consistent and uniform requirements for financial audits of state and local governments, nonprofit organizations, and other recipients of federal assistance; specify standard financial audit requirements for federal assistance programs; and have federal agencies and departments in planning and performing additional work, to the maximum extent feasible, rely upon and not duplicate work done pursuant to S. 1510. See, section 7501 of S. 1510. Specifically, the bill would generally require each recipient of federal assistance of $25,000 or more to conduct, at least biennially, but preferably annually, a single financial audit covering all of its funds. See, section 7504(a)(1).

The purposes of the Inspector General Act, on the other hand, are, in relevant part, to establish Inspectors General in several departments and agencies and authorize them to conduct and supervise audits and investigations of programs and operations of those federal entities. See, section 2 of P.L. 95–452. The Act itself imposes no specific audit requirements.

Two provisions of S. 1510 expressly appear to preclude the possibility of conflict with audit requirements imposed by the bill and any audits which an Inspector General may wish to conduct in the exercise of his judgment. The first provision is section 7504(c) which states that:

"This chapter does not limit the authority of Federal agencies and departments to conduct, or contract for audits and evaluations of Federal assistance programs. This work includes, but is not limited to, economy and efficiency audits, program results audits, and program evaluations, and audit requirements contained in Office of Management and Budget circulars such as A–102, Attachment P. However, in planning and performing any additional work, the Federal agencies and departments, to the extent feasible, shall rely upon and not dupli-

cate the single financial audit. Additional work performed by or for the Federal Executive agencies and departments shall be coordinated by the cognizant agency for the entity in order to coincide, to the extent feasible, with the performance of the single financial audit. The requesting Federal agency or department must arrange for funding the cost of such additional work."

The second provision is section 7508(a) which provides that:

"*Relationship to other law*

"Notwithstanding any other provision of law, unless this section is expressly referred to, single financial audits conducted in accordance with the requirements of this Act shall be deemed to be in lieu of any other financial audit requirement imposed on the entity by the Federal Government. The Comptroller General shall determine the extent to which a particular audit requirement is a financial audit requirement. Nothing in this chapter nor any determination by the Comptroller General shall relieve Federal agencies of their responsibilities to perform other audits, such as economy and efficiency audits or program result audits, or affect their authority to perform audits of Federal assistance recipients and the programs administered by such recipients."

THOMAS J. NICOLA,
Legislative Attorney,
American Law Division.

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